

Historical Background LIHTC and USDA Rural Development

The USDA Rural Development 515 program has about 700 developments comprising 18,000 units in the State of Michigan. The federal budget for this program has been cut dramatically. There hardly exist any funds at all for new development. This year there may be \$27 million available on a national level. There is about the same amount available for rehabilitation of these properties on a national level but most of that money is used for properties that have been foreclosed by the agency and are in inventory.

The LIHTC Program was instituted in 1986. Early in the program in Michigan there was a set aside for Rural Development 515 for both new construction and rehabilitation of 10% of the annual allocation for the State. Initially the entire set aside was not completely used. This was not unusual because the annual allocation was not completely used either. The program was new and those who were using it were trying to figure out how best to use this program to construct and preserve Rural Development assets. The set aside was reduced to 5% in succeeding years.

More recently the definition of **rural** has been changed to include virtually everything that is not urban. This encompasses many more areas and dramatically increases competition for limited dollars available for this program.

Making Rural Development Preservation deals work is much more difficult these days for many reasons. We have the "old and cold" issue which has surfaced lately. This issue makes it impossible for Rural Development to give new rates and terms to borrowers trying to preserve Rural Development 515 housing. We are not able to write down debt or re-amortize existing loans if we want to use the 9% credit. The only avenue left to rehabilitate these properties is the use of the LIHTC. Additionally most of the RD properties with 100% rental assistance have been rehabilitated, leaving only properties with partial or no rental assistance. These deals are much more difficult to do because these rehab efforts almost always need additional debt layered on them to accomplish all that needs to be done. Without the availability to raise rents for the repayment of the additional debt these deals are jeopardized. Again without the use of LIHTC these deals could never be accomplished in the first place. It takes many tools to preserve rural housing. The best tool we have now is the 9% LIHTC.

Two of the reasons that these 515 deals are very difficult to preserve is the debt structure and the rents we are able to attain in the rural communities. RD 515 loans have an interest credit which essentially brings the interest rate down to 1%. When we do a rehab on one of these properties you cannot add much new debt at 8% to replace the 1% money in the deal. The equity from the LIHTC is essential to make the deal work. Market rents in these rural towns are substantially lower than comparable rents in urban areas. Most of our one bedroom units rent for between \$340 - \$375 per month. The two bedroom units average around \$450 per month. That is what the market will allow us to charge. There

is not much room for rents to increase. On a good year in these markets we might get a \$10 increase.

Preservation is the bulk of the work that needs to be done in Michigan as the budget for new construction is nearly nonexistent and most market are marginal. The LIHTC Program is needed to preserve this portfolio.

Suggestions for the QAP—These suggestions are meant as separate ideas not as a cumulative solution. Although that is not to say that more than one of these suggestion could be used toward this end.

Reinstate the full 10% set aside for USDA Rural Development Properties.

Restrict the definition of Rural. Bring it back in line to serve the population that it was initially set up for, population centers of 20,000 or less or 515 properties.

Restrict any project to no more than 15% - 20% of the set aside.

Give preference to applications that have a better use of credit dollar for dollar for accomplishing preservation goals. We are able to preserve a 24 unit property in a rural area with a complete rehab for \$75,000 of annual credit, where a similar 24 unit property in an urban area may require \$300,000 or more of annual credit. It would make sense to give more points or preference to an application that is able to preserve 24 units by using substantially less credit (25% in this instance).

Offer more preference to smaller deals that preserve housing using less amounts of credit. Possibly have a tiered program offering more of a preference to small deals and less to medium and even less to larger deals.

These are a few suggestions for preserving housing in the 515 program. Without the LIHTC Program we are able to preserve only a few units annually. It is painfully obviously that we need this program to help USDA and the 515 program.

Remarks submitted by Pete Potterpin.

PK Housing & Management
President, Michigan Rural Development Council